BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
BOCA LAND COMPANY)

Appearances:

For Appellant: A. De Witt Alexander of San Francisco

For Respondent: Frank L. Guerena of San Francisco

O P I N I O N

This is an appeal, pursuant to Section 25 of the Bank and Corporation Franchise Tax Act (Stats. 1929, Chap. 13) from the action of the Franchise Tax Commissioner in proposing an additional tax in the amount of $448.98 based on the net income of Boca Land Company for the year ended December 31, 1928. It is contended (1) that the Appellant was not during 1928, and has not since, been engaged in business so as to be taxable at all under the Act, and (2) even conceding that it is taxable the Commissioner has erred in basing his additional assessment on a larger portion of the dividends received by the Appellant from The Union Ice Company than is justifiable. It appears that the latter corporation does business within and without the state, so that the Appellant is not taxable on the entire dividends received as an owner of its stock and the question of the proper apportionment of this income arises.

Counsel for the Commissioner has objected vigorously to our consideration of whether or not the Appellant is "doing business" within the meaning of the kct, basing his objection upon the proposition that we have no jurisdiction to consider any point which was not raised before the Franchise Tax Commissioner in the first instance. Undoubtedly, it is true that our Board could acquire no jurisdiction to determine the amount of any tax accruing under the Act unless the corporation should fi: perfect an appeal as contemplated by Section 25.

Once jurisdiction has been acquired by the State Board of Equalization, we believe that it becomes the duty of the Board to determine what in its own judgment is the correct amount of the tax. Our reasons for this belief have been discussed fully in our opinion in the matter of the appeal of Miss Saylor Chocolates (filed August 4, 1930) and are touched upon in our opinion in the matter of the Appeal of R. J. Reynolds Tobacco Co. (filed January 19, 1931). Nothing contained in the brief of the Franchise Tax Commissioner on file herein has caused us to change our views previously expressed.

If it is our duty to determine the correct amount of the

tax in a case properly before us on appeal, it would seem plain that we may consider the matter "de novo". Otherwise, our function would resolve itself merely into the determination of a dispute between the Commissioner and a taxpayer, both of whom may be wrong. The primary object of giving our Board jurisdiction of this character must have been to substitute for the judgment of one man--the Commissioner--the judgment of the Board Members as to what is the correct tax liability of a corporatio

As stated by the Appellant, the provisions of this Act relating to appeals to the State Board of Equalization are analogous to those found in Section 272 of the Federal Revenue Act of 1928, and in similar sections of prior Federal Revenue Acts which have provided that the taxpayer may file a petition with the Board of Tax Appeals for a redetermination of the deficienc In the Appeal of E. J. Barry 1 B.T.A. 156, the Board of Tax Appeals overruled the objection that the taxpayer had not protested the deficiency on grounds subsequently urged upon appeal, saying "When a taxpayer brings his case before the Board he proceeds by trial de novo. The record of the case made in the Internal Revenue Bureau is not before the Board except in so far as it may be properly placed in evidence by the taxpayer or by the Commissioner. The Board must decide each case upon the record made at the hearing before it, and, in order that it may properly do so, the taxpayer must be permitted to fully present any questions relating to his tax liability which may be necessary to a correct determination of the deficiency. To say that the taxpayer who brings his case before the Board is limited to questions presented -before the Commissioner, and that the Board in its determination of the case is restricted to a decision of issues raised in the Internal Revenue Bureau would be to deny the taxpayer a full and complete hearing and an open and neutra consideration of his case,"

To the same effect is the language of the decision in the Appeal of Gutterman Strauss Co., 1 B.T.A. 243, 245, in which the Board thus defined its duties:

"This Board was not created for the purpose of reviewing rulings made by the Commissioner but was created for the purpose of determining thecorrectness of deficiencies in tax found by the Commissioner, If the deficiency in tax found by him is greater than the true deficiency the Board has authority to decrease it; if it is less than the true deficiency, the Board has authority to increase it (Appeal of the Hotel De France Co., 1 B.T.A. 28). If a taxpayer can prove to this Board that he is entitled to a deduction from gross income, the deduction will be allowed even though it has never been claimed by the taxpaye at any hearing had before the Commissioner; otherwise it would be impossible for this Board to determine the correct amount of the deficiency."

Again, the Board has said:

"This Board was not created for the sole purpose of reviewing rulings made by the respondent, but was created for a broade

purpose, i.e., of determining the correctness of deficiencies in tax found by the respondent." (E. S. Frischkorn, 7 B.T.A. 431, 438.)

Inasmuch as we are required to determine the correct amount of the tax, we consider these expressions particularly pertinent and shall govern ourselves accordingly.

This brings us to the consideration of whether or not the Appellant was doing business so as to be taxable under the Act. If we should determine that it was not so engaged then there would be no necessity to rule upon the proposition of the dividends received by the Appellant from the Union Ice Company allocable to California since there would be no tax to calculate

There does not appear to be any controversy as to the facts From our investigation of the situation and from data submitted to our Board by the Appellant it appears that the corporate activity of Boca Land Company has consisted in the main of its ownership of shares of stock of the Union Ice Company constituti more than 85% of the book value of its assets. In addition the company has owned some public utility and State of California bonds and a few shares of stock of other corporations, It does not appear to have engaged in any trading activity with these stocks and bonds. The only exception during 1928 or 1929 appears to have been the sale in 1928 of Chase National Bank and Chase Securities Company stock and of United States Treasury certificates, the proceeds from which were immediately reinvested in bonds. These transactions took place prior to the effective date of the Bank and Corporation Franchise Tax Act. (Statutes of 1929, Chapter 13).

The Boca Land Company has maintained no business activity as such, not excepting any extension of credit or guidance of the activities of the Union Ice Company or of any other company, nor has it had any business office other than the use of space together with other corporations in the office of the Union Ice Company. It has acted merely as the conduit for the transmissic of dividends and other income received from its securities to its own stockholders as dividends.

It is apparent that if we should determine that this state of affairs constitutes doing business on the part of Boca Land Company the tax at four per cent "according to or measured by" its net income would fall in the main on dividends received from the Union Ice Company, which is organized under the laws of this state and which has already been required to pay a tax here "according to or measured by" its net income under the same law. In recognition of the fact that the ultimate source of the funds from which a corporation can pay dividends is its business activity the Act provides that there shall be a deducti in computing the net income of a corporation on account of dividends received during the taxable year from income arising out of business done *in* this state. Consequently, the only part of: the dividends received from the Union Ice Company which could be taxed to Boca Land Company would be that portion of the dividends of the Union Ice Company arising from business done outsi

of this state. (Statutes of 1929, Chapter 13, Section 8(h).)

This income could not be taxed directly to the Union Ice Company for the reason that it is not attributable to business done in California. (Statutes of 1929, Chapter 13, Section 10). After deduction of the value of California property owned by the Union Ice Company from its total corporate worth the prorata value of its stock in the hands of the Boca Land Company would be subject to ad valorem taxation to the latter in the City and County of San Francisco under Section 16 of Article XIII of the Constitution and the Political Code sections enacted pursuant thereto. As above indicated, Boca Land Company is purely passive with reference to any dividends coming to it from its stock in the Union Ice Company and engages in *no* corporate activity with reference thereto other than to distribute these funds to its own stockholders.

The practical effect of taxing Boca Land Company "according to or measured by" its net incomederived from these dividends would be to thus tax indirectly the business of the Union Ice Company done in Nevada, which was not taxable directly. At the same time the Boca Land Company would be required to pay a property tax to the City and County of San Francisco on account of the fact that part of the property of the Union Ice Company is located outside of the state. Therefore, we can not share the concern of the Commissioner at the possibility of this income of the Boca Land Company escaping taxation. It has arisen from business in which California has no direct concern and if all the Boca Land Company does with it after receiving it is to distribute it to stockholders, we can scarcely see how Californi has been deprived of any legitimate franchise tax based upon corporate income derived from busine ss in this state if Boca Land Company is not taxed.

We have had occasion to reconsider the question of what constitutes doing business in our opinion in the case of Eyre Investment Company, filed this day, and have referred therein to the decisions of the federal courts on what constitutes "doing business" within the meaning of the federal laws analogous to ours. In our opinion this Appellant has plainly brought itself within the rule announced by the United States District Court in Nunnally Investment Co, v. Rose, 14 Fed. (2d) 189, which was quoted in our opinion in the matter of the Appeal of Eyre Investment Company. The case of Edwards v. Chile Copper Co., 27 U.S.A.F.2, cited by the Commissioner, is inapposite because there the taxpayer was a means of obtaining credit for the subsidiary and "by indirection governed it" so that it was a good deal more than a mere conduit. Nor are we impressed by the reliance which the Commissioner places upon the case of Central Coal and Coke Co. v. Carselowey, 40 Fed. (2d) 540. We have analyzed that decision in our opinion in the matter of the Appeal of Portland California Steamship Co. (filed November 20, 1930) and have shown that it is not determinative of the question of what constitutes "doing business" as it is presented to us under the California statute.

In view of the foregoing considerations, we conclude that Boca Land Company was not doing business within the meaning of the California Bank and Corporation Franchise Tax Act at the time of the proposed assessment. Therefore, it becomes unnecessary for us to consider the proper percentage of the dividends of the Union Ice Company allocable to taxation as derived from business done outside of this state.

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED, AND DECREED, that the action of the Franchise Tax Commissioner in overruling the protest of Boca Land Company, a corporation, against a proposed additional assessment based upon a return of said corporation for the year ended December 31, 1928, under Chapter 13, Statute: of 1929, be and the same is hereby reduced. Said ruling is hereby set aside and said Commissioner is further directed to refund to said corporation any tax collected from it on the basis of said return as provided in Section 27 of said Chapter, all in conformity with the foregoing opinion of this Board.

Done at Sacramento, California, this 11th day of May, 1931, by the State Board of Equalization.

Jno. C. Corbett, Chairman
R, E. Collins, Member
H. G. Cattell, Member
Fred E. Stewart, Member

ATTEST: Dixwell L. Pierce, Secretary